



Update on major anti-money laundering and counter-financing of terrorism regulatory developments

December 2020

Disclaimer and Reminder

Agenda

- I. International and Hong Kong AML/CFT regulatory developments
- II. Counter financing of proliferation of weapons of mass destruction regime
- III. SFC's AML/CFT initiatives
- IV. SFC's findings from inspections of AML/CFT controls and compliance practices

Mitigating ML/TF risks of virtual assets

Hong Kong legislative proposal

To implement the FATF requirements for VASPs, the Government proposes to expand the scope of the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap.615) (AMLO) to apply the customer due diligence and record-keeping obligations under Schedule 2 to the AMLO to VASPs.

A licensing regime for VASPs will be introduced, whereby any person seeking to conduct the business of operating virtual assets trading platforms in Hong Kong will be required to be licensed and supervised by the SFC and subject to fit-and-proper criteria.

Licensed VASPs will be required to observe AML/CFT requirements as well as other regulatory requirements designed for investor protection purposes.



Note: More details of the proposal can be found in the consultation document available on the website of the Financial Services and the Treasury Bureau at https://www.fstb.gov.hk/fsb/ppr/consult/consult_amlo.htm. The public consultation period closes on 31 January 2021.



International and Hong Kong AML/CFT regulatory developments

(1) Mitigating the money laundering and terrorist financing risks of virtual assets

(2) Use of digital identity for customer due diligence

(3) Other proposed AMLO amendments

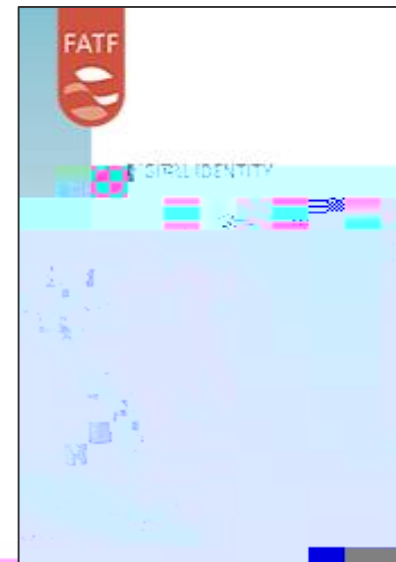
Use of digital identity for customer due diligence

FATF guidance paper on digital identity

Recognises the potential that robust digital identity (digital ID) systems can improve the reliability, security and efficiency of identifying individuals in the financial sector

Sets out the risks and benefits of digital ID, and a decision-making process requirements for customer due diligence

Potential for financial inclusion be increased and human internal control weaknesses be reduced



Use of digital identity for customer due diligence

Hong Kong legislative proposal

The Government proposes to amend section 9 of Schedule 2 to the AMLO to add:

the use of independent and reliable digital identification systems for customer identification and verification purposes as a permissible way to satisfy the special requirements where customer is not physically present for identification purposes.



Note: More details of the proposal can be found in the consultation document available on the website of the Financial Services and the Treasury Bureau at https://www.fstb.gov.hk/fsb/ppr/consult/consult_amlo.htm. The public consultation period closes on 31 January 2021



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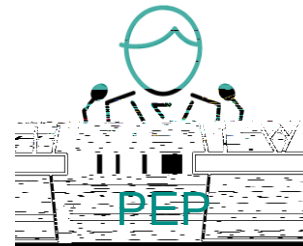
(3) Other proposed AMLO amendments

Other proposed AMLO amendments

Politically exposed persons (PEPs)

To extend the additional measures applicable to foreign PEPs to PEPs in other parts of China outside Hong Kong by amending the definition of PEP under the AMLO

To enable the adoption of a risk-based approach to determine whether to continue to apply the additional measures for foreign PEPs who are no longer entrusted with a prominent public function



Beneficial ownership of trust

To
relation to a trust to include trustees and beneficiaries (including class of beneficiaries)





Counter financing of proliferation of weapons of mass destruction regime

Irene Pou, Associate Director

**Intermediaries Supervision
Intermediaries**

What is financing of proliferation of weapons of mass destruction (proliferation financing)?

FATF Definition –

... **providing funds or financial services** which are used, **in whole or in part**, for the **manufacture, acquisition, possession, development, export, trans-shipment, brokering, transport, transfer, stockpiling or use of nuclear, chemical or biological weapons and their means of delivery and related materials** (including both technologies and dual use goods used for non-legitimate purposes)...



Strengthening measures to prevent proliferation financing

Revision of FATF Recommendation 1 (R.1) and its interpretive note

To require jurisdictions, financial institutions and designated non-financial businesses and professions (DNFBPs) to identify, assess and mitigate the risks of potential breaches, non-implementation or evasion of the targeted financial sanctions related to **proliferation financing**, and to take effective action to mitigate these risks.

Counter proliferation financing regime in Hong Kong

United Nations Security Council
sanctions against
the Democratic People's Republic
of Korea ("DPRK") and Iran



Targeted Financial Sanctions against
designated individuals and entities
**United Nations Sanctions
Ordinance (Cap.537)**



**United Nations
Sanctions
(DPRK) Regulation
(Cap. 537AE)**

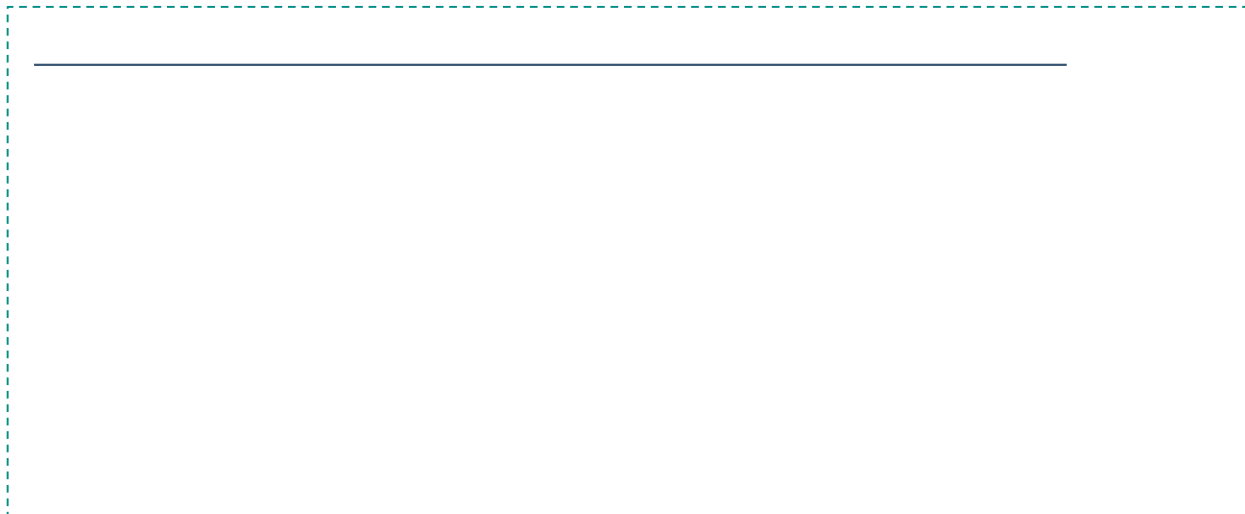


**United Nations
Sanctions
(JCPOA - Iran) Regulation
(Cap.537BV)**

**Weapons of Mass
Destruction (Control of Provision
of Services) Ordinance
(Cap.526)**



Counter proliferation financing regime in Hong Kong



Actions to mitigate proliferation financing risks



Should not establish business relationship or conduct transactions with sanctioned individuals or entities.



Should implement an effective screening mechanism, which should include screening customers and their



SFC's AML/CFT initiatives

- (1) ML/TF risk assessment of the Hong Kong securities sector
 - (2) Public consultation on proposed amendments to AML/CFT guidelines
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Irene Pou, Associate Director

Intermediaries Supervision
Intermediaries

ML/TF risk assessment of Hong Kong securities sector

FATF Recommendation 1 requires jurisdictions to:

- identify, assess and understand the ML/TF risks to which the jurisdiction is exposed; and
- keep their risk assessment up-to-date

The Government published the first ML/TF risk assessment report in 2018

The SFC is in the process of conducting an assessment to identify the latest ML/TF risks of the securities sector of Hong Kong is exposed, which will

assessment report to be published





SFC's AML/CFT initiatives

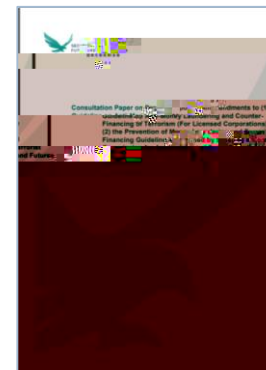
(1) ML/TF risk assessment of the Hong Kong securities sector

(2) Public consultation on proposed amendments to AML/CFT guidelines

Background and objectives

On 18 September 2020, the SFC launched a three-month public consultation on proposals to amend its AML/CFT guidelines

The key proposed amendments aim to achieve the following objectives:



Business relationships established or transactions conducted by customers through channels that are less susceptible to ML/TF risk such as that related to unauthorised trading and fraud

Lower risk

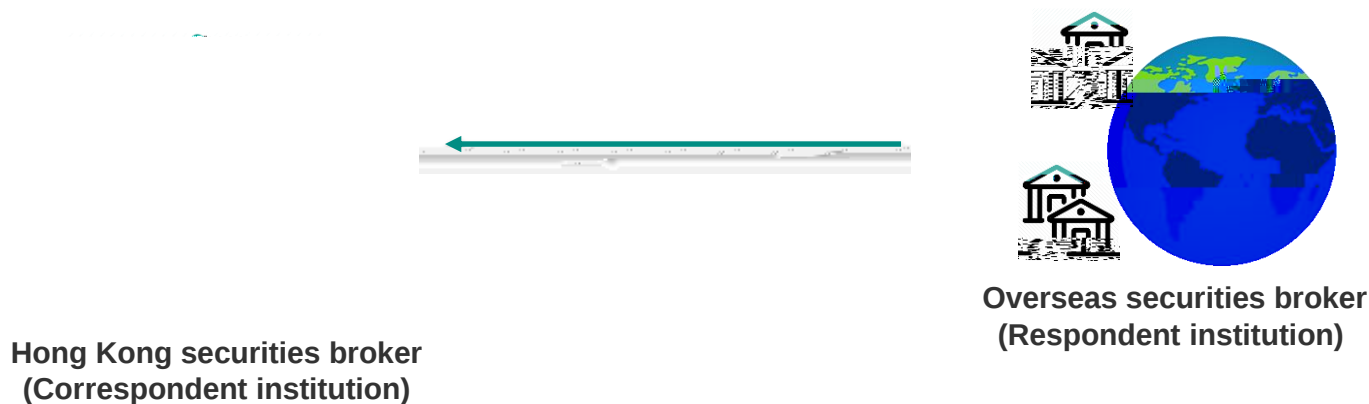
Non-resident customers who have no discernible reason for opening an account with FIs in Hong Kong instead of

jurisdiction

Securities-related products or services funded by payments from or instructions given by unexpected third parties, particularly from jurisdictions posing higher risk

Higher risk

Example of cross-border correspondent relationship in the securities sector:



Scope of application

The provision of services to an overseas financial institution for conducting transactions that constitute:

- Type 1 regulated activity: dealing in securities;
- Type 2 regulated activity: dealing in futures contracts; or
- Type 3 regulated activity: leveraged foreign exchange trading.



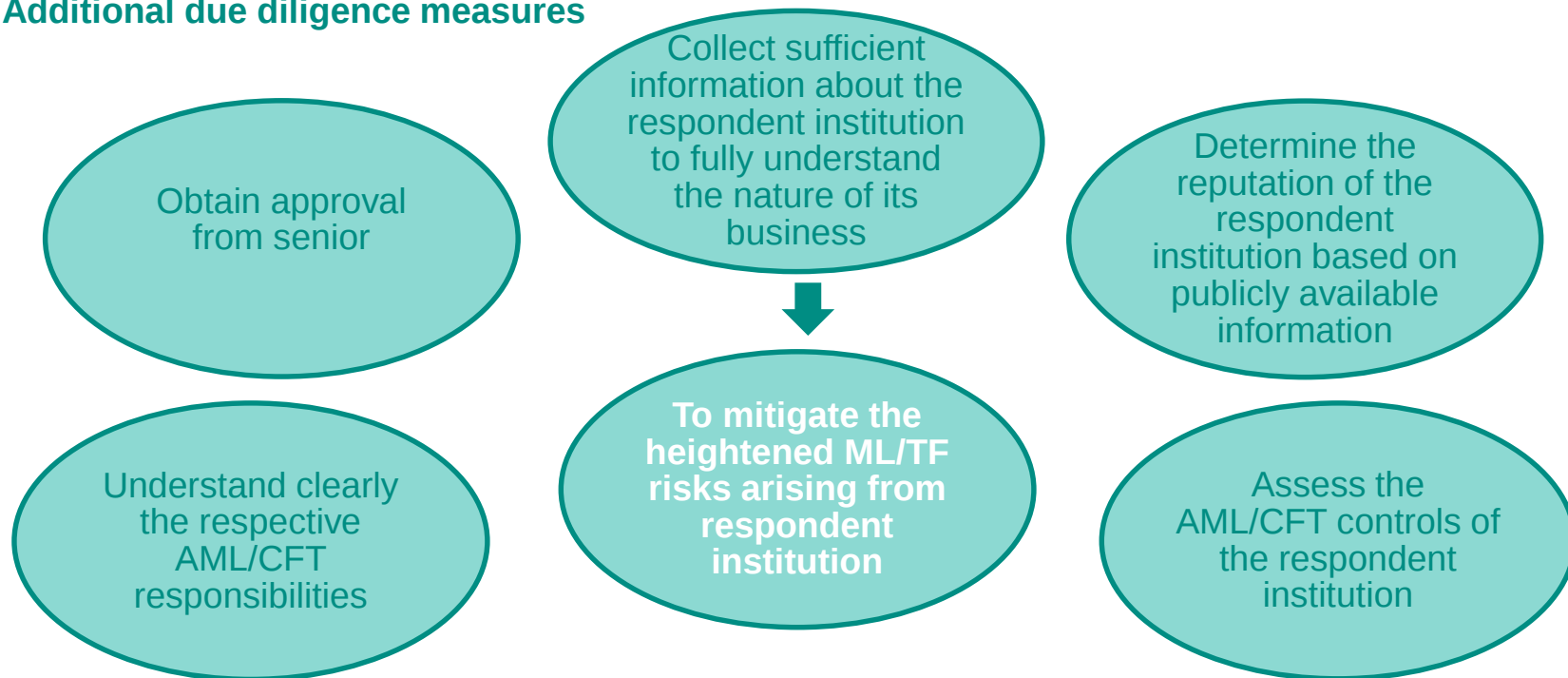
Proposed amendments – Cross-border correspondent relationships



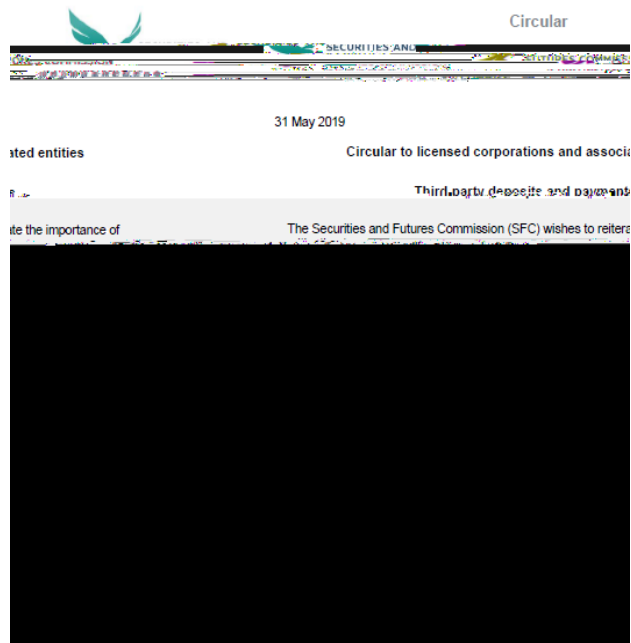
FATF Recommendation 13

requires correspondent institutions to perform **additional due diligence measures** and other risk mitigating measures; applicability to the securities sector is elucidated
-based Approach for the Securities Sector

Additional due diligence measures



Proposed amendments - Third-party deposits and payments



Incorporate existing guidance provided in circulars

Provide additional facilitative guidance relating to third-party deposits to address industry feedback

Existing guidance for facilitating prompt identification of the source of deposits:

Inform clients in writing of policies for handling third-party deposits and payments

Encourage the deposit of funds by clients only through designated bank accounts

of any acceptable third parties) for facilitating easy identification of the source

Proposed amendments – Delayed third-party deposit due diligence





SFC's findings from inspections of AML/CFT controls and compliance practices

Sharon Wong, Manager

**Intermediaries Supervision
Intermediaries**

SFC's findings from inspections of AML/CFT controls and compliance practices

1. Implementing comprehensive and up-to-date policies and procedures, and maintaining adequate oversight and internal controls for ensuring the proper and effective performance of AML/CFT functions by staff
2. Considering pertinent ML/TF risk factors when conducting institutional and customer risk assessments, as well as following up on the assessment results
3. Assessing fund deposits by clients to ascertain whether they originate from third party payors in order to apply appropriate due diligence and transaction monitoring measures
4. Establishing source of wealth and source of funds for high-risk customers
5. Screening existing customers, their beneficial owners and other relevant connected parties

Example of deficiencies and non-compliance in the critical areas identified by our inspection

Internal control and governance

Failed to update their **policies and procedures** promptly to ensure they remain up-to-date and relevant after amendments were made to the AMLO and AML/CFT Guideline in 2018



Failed to provide sufficient information for **senior management** to maintain

Accumulated backlogs of sanctions screening and transaction alerts pending for review;
Delays in performance of periodic reviews of customer information

Example of deficiencies and non-compliance in the critical areas identified by our inspection

ML/TF risk assessments



Inadequate consideration of all key, relevant ML/TF risk factors in **institutional risk assessment** and **customer risk assessment** processes

Simply made reference to a list of jurisdictions identified by the FATF as having strategic deficiencies in their AML/CFT regimes
Deemed all countries which are a member jurisdiction of a FATF-style regional body as non-high risk without conducting a proper assessment

Transaction monitoring systems and processes

Not all fund deposits by clients were assessed to ascertain whether they came from third party payors
diligence and transaction review processes



Example of deficiencies and non-compliance in the critical areas identified by our inspection

SFC's findings from inspections of AML/CFT controls and compliance practices

To properly discharge their role, senior management should ensure, among other actions,:

1. appropriate mechanisms are in place to develop and continuously review procedures;
2. adequate training tailored to their specific job functions and

Thank you

AML/CFT section of the SFC website:

<https://www.sfc.hk/en/Rules-and-standards/Anti-money-laundering-and-counter-financing-of-terrorism>